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Nos. 08-240 & 08-372

Supreme Court, U.S.
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IN THE
Supreme Court of the United States

MAC'S SHELL SERVICE, INC., ET AL.,

Petitioners,

v.

SHELL OIL PRODUCTS COMPANY LLC, ET AL.,

Respondents.

SHELL OIL PRODUCTS COMPANY LLC, ET AL.,

Petitioners,

v.

MAC'S SHELL SERVICE, INC., ET AL.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE AMERICAN PETROLEUM INSTITUTE AS *AMICUS CURIAE* SUPPORTING SHELL OIL PRODUCTS COMPANY LLC, MOTIVA ENTERPRISES LLC AND SHELL OIL COMPANY, INC.

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INTEREST OF *AMICUS CURIAE*

The American Petroleum Institute ("API") is a non-profit District of Columbia corporation that represents the United States oil and natural gas industry.[1] API's more than 400 members cover all facets of the industry, including exploration, production, transportation, refining, and marketing.

API's members have a significant interest in the issue in this case. The Petroleum Marketing Practices Act, 15 U.S.C. §§ 2801-2807 ("PMPA" or "the Act"), establishes federal standards for the termination or non-renewal by an oil refiner of a service station dealer's franchise. The PMPA provides dealers with a cause of action against oil refiners that terminate a franchise or fail to renew it in a manner that violates the statute. Thus, many of API's members are subject to suit under the Act.

This case presents the question whether a service station dealer that continues to operate its franchise may nevertheless sue the franchisor for wrongful "termination" or "nonrenewal" under the PMPA. The First Circuit held that a service station operator can maintain a suit for constructive termination, but the text, structure, and purpose of the statute make clear that the First Circuit erred in

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[1] Pursuant to Rule 37.6, *amicus* affirms that no counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus*, its members, or its counsel made a monetary contribution to its preparation or submission. The parties have consented in writing to the filing of this brief.

according the PMPA such broad scope. Because API members may be subjected to PMPA suits, they have a strong interest in limiting the statute to the circumstances in which Congress intended it to apply.

API frequently participates in legislative, administrative, and judicial proceedings that present issues of national concern, including issues arising under the PMPA.[2] API believes that its participation as *amicus curiae* in this case will offer the Court an industry-wide perspective on the question presented.

STATEMENT

1. Congress enacted the PMPA to establish "minimum federal standards governing the termination and nonrenewal of franchise relationships for the sale of motor fuel by the franchisor or supplier of such fuel." S. Rep. No. 731, 95th Cong., 2d Sess. at 15 (1978). Congress sought to displace "an uneven patchwork of [state] rules governing franchise relationships" with a "single, uniform set of rules governing the grounds for termination and non-renewal . . . and the notice which franchisors must provide franchisees prior to termination of a franchise or non-renewal." *Id.* at 19. To promote "certainty and uniformity in franchise relationships which permeate a nationwide motor fuel distribution and marketing network," the PMPA

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[2] *See, e.g., Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007); *Bell Atl. Corp. v. Twombly*, 550 U.S. 544 (2007); *Texaco, Inc. v. Dagher*, 547 U.S. 1 (2006); *Texaco, Inc. v. Hasbrouck*, 496 U.S. 543 (1990).

"preempts state law in the subject areas in which the federal legislation deals, i.e., termination and non-renewal of franchise relationships and the notice applicable thereto," if the state law "is not the same as the applicable provision" of the PMPA. *Id.* at 16. *See* 15 U.S.C. § 2806(a)(1).

The PMPA defines a "franchise" to mean the use by a franchisee of "a trademark which is owned or controlled by" a refiner "in connection with the sale, consignment, or distribution of motor fuel." 15 U.S.C. § 2801(1)(A). "Franchise" is also defined to include a contract for the supply of motor fuel or a lease of the premises on which the motor fuel is sold "under a trademark which is owned or controlled by" the refiner. *Id.* § 2801(1)(B). Courts refer to these three components of the franchise as the "statutory element[s]" of the franchise. Pet. App. 18a. "Franchise" is further defined to include "the unexpired portion of any franchise, . . .which is transferred or assigned as authorized by the provisions of such franchise or by any applicable provision of State law which permits such transfer or assignment without regard to any provision of the franchise." 15 U.S.C. § 2801(1)(B)(iii).

In setting federal standards for termination of a franchise, Congress attempted to "strike a balance between" (S. Rep. No. 731, at 15) franchisees' interest in avoiding "arbitrary or discriminatory termination" (*id.*) and franchisors' need for "adequate flexibility" to "initiate changes in their marketing activities to respond to changing market conditions and consumer preferences" (*id.* at 19). Concerned about franchisors "resort[ing] to termination of the franchise for the most technical or minor violations

of the contract" (*id.* at 18), Congress enumerated the grounds on which the franchisor may lawfully terminate the franchise. *See* 15 U.S.C. § 2802(b)(2). Those grounds include a failure by the franchisee to comply with a franchise provision that "is both reasonable and of material significance," *id.* § 2802(b)(2)(A); "[a] failure by the franchisee to exert good faith efforts to carry out" the franchise, *id.* § 2802(b)(2)(B); "[t]he occurrence of an event which is relevant to the franchise relationship" and which renders termination of the franchise "reasonable," *id.* § 2802(b)(2)(C); a written agreement between the franchisor and franchisee to terminate the franchise, *id.* § 2802(b)(2)(D); and a "determination made by the franchisor in good faith and in the normal course of business to withdraw from the marketing of motor fuel through retail outlets in the relevant geographic market," *id.* § 2802(b)(2)(E).[3]

Congress also sought to ensure that procedural regularity attends the termination process by imposing notification requirements on franchisors. *See* 15 U.S.C. § 2804. The PMPA requires that the franchisor notify the franchisee in writing of the date on which termination will take effect and the reasons for which the franchise is being terminated. *Id.* § 2804(c). That notice must

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[3] The listed grounds for termination are also grounds for non-renewal. Section 2802(b)(3) sets out additional grounds for non-renewal, including the failure of the parties "to agree to changes or additions to the provisions of the franchise" if the changes or additions "are the result of determinations made by the franchisor in good faith and in the normal course of business." 15 U.S.C. § 2802(b)(3)(A).

generally be provided at least 90 days before the date termination "takes effect." *Id.* § 2804(a)(2).

The PMPA provides franchisees with a cause of action against a franchisor that fails to comply with the statute's provisions governing termination or non-renewal. 15 U.S.C. § 2805(a). It directs a court to grant a franchisee a preliminary injunction to compel continuation or renewal of the franchise relationship while the court considers the merits of the franchisee's challenge to the franchisor's termination or non-renewal, provided certain specified conditions are met. *Id.* § 2805(b). The franchisee need only establish "sufficiently serious questions going to the merits to make such questions a fair ground for litigation" and that the balance of hardships tips in its favor. *Id.* § 2805(b)(2). The statute authorizes prevailing franchisees to recover actual damages and, in cases involving "willful disregard" of the statute, punitive damages. *Id.* § 2805(d)(1)(A), (B). Franchisees are also entitled to "reasonable attorney and expert witness fees" unless the franchisee recovers "only nominal damages," in which case such fees may be awarded in the court's discretion. *Id.* § 2805(d)(1)(C).

The PMPA contains two provisions addressing the statute's relationship with state law. The first provision provides that "no State or any political subdivision thereof may adopt, enforce, or continue in effect any provision of any law or regulation . . . with respect to termination . . . of any such franchise or to the nonrenewal . . . of any such franchise relationship unless such provision of such law or regulation is the same as the applicable provision of this subchapter." 15 U.S.C. § 2806(a)(1).

The second provision addresses assignments of the franchise and provides that "[n]othing in this subchapter authorizes any transfer or assignment of any franchise or prohibits any transfer or assignment of any franchise as authorized by the provisions of such franchise or by any applicable provision of State law which permits such transfer or assignment without regard to any provision of the franchise." *Id.* § 2806(b)(1).

2. Despite the fact that the PMPA by its terms applies only to "termination" or "non-renewal" of the franchise, the plaintiffs, Shell service station operators in Massachusetts (the "dealers"), sued Shell Oil Company, Inc., and its assignee, Motiva Enterprises LLC (collectively, "Shell") under the PMPA while signing new agreements and continuing to operate their franchises. They did so on the theory that Shell's elimination of a rent reduction program and other changes to the manner of computing rent amounted to "constructive termination" and "constructive[] nonrenew[al]"of the franchises. Pet. App. 4a.[4] The jury returned a verdict in the dealers' favor, awarding them $1.3 million on their constructive termination claim and $1.2 million on their constructive nonrenewal claim. The district court added $1.16 million in attorney's fees and $209,000 in expert witness fees pursuant to the PMPA.

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[4] Specifically, the dealers alleged that Shell Oil Company constructively terminated their franchises by assigning the franchises to Motiva Enterprises LLC, which canceled the rent subsidy. Pet. App. 4a

3. The court of appeals affirmed in part and reversed in part. Pet. App. 15a-25a. The court held that the PMPA provides a cause of action for constructive termination but not for constructive nonrenewal.

On the constructive termination claim, the court held that a dealer that continues to operate the franchise—that is, continues to use the refiner's trademark, to receive motor fuel, and to lease the premises—can nevertheless claim that it was "terminated" within the meaning of the PMPA. Pet. App. 17a-18a. In so holding, the court relied on the Fourth Circuit's decision in *Barnes v. Gulf Oil Corp.*, 795 F.2d 358 (4th Cir. 1986), which held that a constructive termination claim under the PMPA is available even when the franchisee continues to operate its business if an assignment of the franchise either (1) violates state law or (2) results in a breach of one of the three statutory elements of the franchise. Pet. App. 15a-18a.

The court of appeals concluded that constructive termination under the PMPA, unlike constructive termination in several other contexts, does not "require an actual severance of the relationship." *Id.* at 18a. The court reasoned that "requiring a franchisee to go out of business before invoking the protections of the PMPA" would frustrate the "congressional plan." *Id.* (internal quotation marks omitted). Instead, the court held that the PMPA provides a cause of action for constructive termination where a franchisee alleges both that the franchisor (or its assignee) breached one of the three statutorily protected contracts—the contract for use of the trademark, motor fuel, or the

premises—and that the breach is "such a material change that it effectively ended the lease, even though the [franchisees] continued to operate the business." *Id.* (internal quotation marks omitted).

The court of appeals agreed with Shell, however, that the PMPA does not provide a cause of action for constructive nonrenewal. Pet. App. 21a-25a. The court noted that while the Ninth Circuit recognized such a claim in *Pro Sales, Inc. v. Texaco, U.S.A.*, 792 F.2d 1394 (9th Cir. 1986), that decision "has been rejected by the other circuits to consider the issue." Pet. App. 22a. The court observed that a constructive nonrenewal theory is inconsistent with the text of the PMPA, which "after all, requires a franchisor to provide a notice of nonrenewal, 15 U.S.C. § 2805(c), and then provides a framework for the franchisee to seek preliminary relief on receipt of that notice, *id.* § 2805(b)(2)." Pet. App. 22a. The court further observed that the Fifth and Seventh Circuits have held that the PMPA's "notice-and-preliminary-relief structure" reflects Congress's intent "to limit the reach of the PMPA to cases where either a notice is given or an actual nonrenewal has taken place." *Id.* (citing *Abrams Shell v. Shell Oil Co.*, 343 F.3d 482, 489 & n.16 (5th Cir. 2003), and *Dersch Energies, Inc. v. Shell Oil Co.*, 314 F.3d 846, 865-66 (7th Cir. 2002)). The court thus declined to "recognize a claim for nonrenewal under the PMPA where the franchisee has signed and operates under the renewal agreement complained of." *Id.* at 25a.

SUMMARY OF ARGUMENT

The court of appeals' decision to recognize a cause of action for constructive termination

misconstrues the scope of the PMPA. The PMPA defines a franchise to include the contracts between the refiner and the dealer that authorize the dealer to use the refiner's trademark, sell the refiner's motor fuel, and occupy leased marketing premises. 15 U.S.C. § 2801(B)(i), (ii). The text of the PMPA makes clear that a franchisor must terminate a franchise, or notify the franchisee of its intent to terminate the franchise, before a franchisee has a cognizable claim for wrongful termination. Read together, the substantive and procedural provisions governing termination do not support the court of appeals' recognition of a cause of action for alleged material breaches of the franchise that fall short of termination.

The court of appeals justified its departure from the text of the Act on the ground that requiring termination of the franchise would frustrate the "congressional plan" to protect franchisees' investment in their businesses. Pet. App. 18a. The court's reasoning lacks merit. First, the best evidence of Congress's intent is the text of the statute, which does not authorize causes of action challenging a franchisor's decision merely to change the terms of the franchise. Second, the remedial plan Congress adopted allows a franchisee threatened with termination to obtain a preliminary injunction compelling continuation of the franchise while a court examines the grounds on which the franchisor intends to effect termination. Moreover, state law causes of action remain available to remedy alleged breaches of contract that do not involve termination of the franchise. By allowing franchisees to sue for breach of contract under the

PMPA, the court of appeals has broadened the scope of the federal regime well beyond what Congress intended.

The court of appeals' approach frustrates the uniform national regime that Congress sought to establish for the termination and nonrenewal of petroleum franchises. Under the court of appeals' decision, determining whether a constructive termination occurred will often turn on the application of *state* law, as it did here. The court of appeals upheld a decision that Shell breached an oral promise to continue the rent subsidy despite a clause in the lease agreement (the "integration clause") providing that the lease constituted the entire contract and could be amended only in writing. The court of appeals concluded that under Massachusetts law, "the question of integration is one of fact reserved for the trial judge" (Pet. App. 13a) and that the judge did not commit clear error in "conclud[ing] that the lease was not an integrated agreement." *Id.* at 14a. Having determined that the oral agreement was enforceable, the court of appeals held that by breaching it, Shell effected a constructive termination under the PMPA. Thus, the success of the dealers' claim that they were constructively terminated turned on an application of state law, an outcome contrary to Congress's desire to establish a "uniform" (S. Rep. No. 731, at 19) and "federal" standard (*id.* at 15) for the termination of petroleum franchise relationships.

The court of appeals' flawed approach can be traced to the Fourth Circuit's opinion in *Barnes v. Gulf Oil Corp.*, 795 F.2d 358 (4th Cir. 1986). That decision recognized two grounds for a claim of

wrongful termination where, as in this case, there has been an assignment of the franchise. The *Barnes* court held that the franchisee could establish that her franchise had been terminated under the PMPA by showing either that the price term in the contract for gasoline supply was breached or that the franchise was assigned in violation of state law. 795 F.2d at 362-64. Neither ground has support in the text of the Act; both expand the PMPA well beyond its intended scope and destroy uniformity in the law governing the termination of petroleum franchises.

For the same reasons that the court of appeals erred in recognizing a cause of action for constructive termination, the court of appeals correctly rejected the dealers' claims for constructive nonrenewal. The substantive, procedural, and remedial provisions of the PMPA governing nonrenewal are parallel to the provisions governing termination. Properly construed, those provisions provide a cause of action for nonrenewal only where "a notice [of nonrenewal] is given or an actual nonrenewal has taken place." Pet. App. 22a.

ARGUMENT

I. The PMPA Does Not Create A Cause Of Action For Constructive Termination.

The PMPA does not provide a cause of action for constructive termination. In recognizing a cause of action under the PMPA for material changes to the franchise that are adverse to the franchisee, the court of appeals deviated from the language and structure of the Act, which creates a cause of action for wrongful termination only when the franchisor

has actually terminated the franchise or notified the franchisee of its intent to do so.

A. The Text and Structure of the PMPA Do Not Allow a Cause of Action for Constructive Termination.

The PMPA defines a franchise to mean the use by a franchisee of "a trademark which is owned or controlled by" a refiner "in connection with the sale, consignment, or distribution of motor fuel." 15 U.S.C. § 2801(1)(A). "Franchise" is also defined to include a contract for the supply of motor fuel or a lease of the premises on which the motor fuel is sold "under a trademark which is owned or controlled by" the refiner. *Id.* § 2801(1)(B). The PMPA does not define the term "termination," other than to state that the term includes "cancellation." 15 U.S.C. § 2801(17). "Termination" is ordinarily understood to mean "end in time or existence: close, cessation, conclusion." Webster's Third New International Dictionary 2359 (1993). If Congress had intended the term to cover a much broader range of conduct that is not commonly understood as "termination," it is fair to assume Congress would have said so. Moreover, the PMPA's provisions governing the grounds for termination and its notification requirements confirm that the Act provides a remedy only for a franchisor's decision to terminate the franchise.

The PMPA enumerates several grounds on which a franchisor may lawfully terminate the franchise, all of which presuppose that termination involves an end to the franchise (*i.e.*, to the use of the

trademark, to the supply of motor fuel, or to the lease of the premises, *see* 15 U.S.C. § 2801(B)), and not merely a change to the franchise terms that has adverse financial consequences for the franchisee. *See* 15 U.S.C. § 2802(b)(2)(A) (franchisor may terminate franchise if franchisee fails to comply with a reasonable and materially significant franchise term if franchisor knew about failure in specified time period preceding notification of termination); *id.* § 2802(b)(2)(B) (franchisor may terminate franchise if franchisee fails to "exert good faith efforts to carry out the provisions of the franchise" if failure continues into specified time period preceding notification of termination); *id.* § 2802(b)(2)(C) (franchisor may terminate franchise based on occurrence of an event relevant to the franchise relationship and that renders termination reasonable, provided the event occurred while the franchise was still in effect and franchisor knew of the event in specified time period preceding notification of termination); *id.* § 2802(b)(2)(D) (franchisor may terminate franchise based on written agreement between the franchisor and franchisee to terminate the franchise); *id.* § 2802(b)(2)(E) (franchisor may terminate franchise based on good-faith determination in the normal course of business to withdraw from the marketing of motor fuel through retail outlets in the relevant geographic market). These provisions contemplate a termination of the franchise, initiated by the franchisor, and set out acceptable reasons for it.[5]

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[5] As explained in note 3, *supra*, a franchisor may refuse to renew a franchise relationship on the same grounds, and (continued...)

The PMPA also contains a highly structured notice procedure that reinforces the conclusion that termination under the Act means a decision by the franchisor to terminate the franchise, not merely a decision to change the terms of the franchise in a manner adverse to the franchisee. The PMPA generally requires the franchisor to provide written notice of its intent to terminate the franchise at least "90 days prior to the date on which such termination or nonrenewal takes effect." 15 U.S.C. § 2804(a)(2). If a franchisor terminates the franchise without providing the requisite notice, the franchisee may sue under the PMPA for a violation of Section 2802. *See id.* § 2805(a); *id.* § 2802(b)(1)(A).

Under the court of appeals' rule that a claim for constructive termination lies where a breach of a franchise term is serious enough to "effectively end[] the lease, even though the plaintiffs continued to operate the business" (Pet. App. 18a), the notice requirement becomes unworkable, because the franchisor will not necessarily know whether or when a change in the franchise terms will "effectively [but not actually] end[] the lease." *Id.* The notice provisions thus operate together with the provisions setting out the legitimate grounds for termination to regulate the franchisor's decision to terminate the franchise, not merely to change the franchise terms in a manner that has an adverse effect on the franchisee.

Section 2802(b)(3) provides additional grounds for nonrenewal.

The PMPA provides a cause of action against franchisors that "fail[] to comply with the requirements of section 2802." 15 U.S.C. § 2805(a).[6] As discussed above, Section 2802 is concerned exclusively with a decision by a franchisor to sever its relationship with the franchisee either through termination or non-renewal of the franchise relationship. Because Section 2805(a) cross-references Section 2802 to define the cause of action, the cause of action that Section 2805(a) creates for failure to comply with the termination provisions extends only to termination or threatened termination of a franchise that the franchisee contends is not justified by the grounds enumerated in Section 2802. It does not encompass the dealers' claim that Shell breached the rent term of the lease. *See Abrams Shell v. Shell Oil Co.*, 216 F. Supp. 2d 634, 639 (S.D. Tex. 2002) (rejecting constructive termination theory under the PMPA "because it conflicts with the PMPA's remedial scheme"), *aff'd*, 343 F.3d 482 (5th Cir. 2003).

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[6] The PMPA also provides a cause of action against a franchisor that fails to comply with the requirements of Section 2803, which provides special rules for the nonrenewal of "[t]rial and interim franchises," 15 U.S.C. § 2803, or with the requirements of Section 2807, which prohibits franchisors from imposing certain restrictions relating to the installation of a renewable fuel pump or the sale of renewable fuel.

B. The PMPA's Remedial Provisions Allow Franchisees to Protect Their Franchise When Threatened With Termination.

The court of appeals justified its ruling on the ground that "[t]he congressional plan would be frustrated by requiring a franchisee to go out of business before invoking the protections of the PMPA." Pet. App. 18a (internal quotation marks omitted). But the best evidence of Congress's intent is the text of the statute, *see West Virginia Univ. Hosps., Inc. v. Casey*, 499 U.S. 83, 98 (1991), which provides no support for the theory that changes to terms of the franchise short of termination are governed by the PMPA. Moreover, the PMPA includes provisions that permit a franchisee to challenge a franchisor's decision to terminate the franchise without relinquishing the franchise. Those provisions impose notice requirements on franchisors who intend to terminate the franchise, 15 U.S.C. § 2804, and permit franchisees to file suit and obtain a preliminary injunction compelling continuation or renewal of the franchise relationship while the merits of the franchisee's challenge are being litigated. *Id.* § 2805(b). Congress even relaxed the traditional equitable standards, requiring the granting of a preliminary injunction on a franchisee's showing merely that "there exist sufficiently serious questions going to the merits to make such questions a fair ground for litigation" and that the balance of hardships tips in its favor. *Id.* § 2805(b)(2).

As the Seventh Circuit has explained, the PMPA's notice requirements, together with the "lenient standard" for injunctive relief, "protect[] franchisees not only from arbitrary and discriminatory termination or nonrenewal, but also from the harmful effects of threatened termination or nonrenewal." *Dersch Energies, Inc. v. Shell Oil Co.*, 314 F.3d 846, 863 (7th Cir. 2002). That is so because under the Act, "the district court is required to issue an injunction to protect the franchisee's economic interests during the pendency of the case" if the franchisee meets the Act's "lenient standard." *Id.* at 865.

The remedial scheme Congress established thus provides a means for franchisees to protect their franchises while challenging a planned termination. Moreover, state law causes of action remain available to protect franchisees that allege that the franchisor committed a breach of contract short of termination of the franchise. Indeed, in this very case the dealers brought state law causes of action that were duplicative of their PMPA claims. *See* Pet. App. 37a (Judgment ¶ 2(v)) ("Because plaintiff's claims under Count II (Violation of the PMPA based on Constructive Termination of the franchise relationship) and under Count V (Breach of the Lease) sought the same damages for loss of the STIP subsidy and lost business value and the jury awarded the same damages, plaintiff is entitled to recover as to those two awards only once."); *id.* at 39a; 40a; 42a; 44a; 46a; 48a; 50a; 52a. The text and structure of the PMPA provide no support for the court of appeals' recognition of a cause of action for alleged material breaches of the franchise that do not

result in termination, a holding that federalizes ordinary breach of contract claims that are the traditional province of state law.

II. Permitting A Claim For Constructive Termination Based On A Material Breach Of Franchise Terms Frustrates The Uniformity Congress Sought To Establish By Enacting The PMPA.

Congress enacted the PMPA to establish a uniform, federal standard to govern the termination and non-renewal of petroleum franchise relationships. A uniform approach is crucial to the effective operation of the national market for motor fuel distribution. The court of appeals' recognition of a cause of action under the PMPA for constructive termination is not compatible with the congressional goal of uniformity because the determination of whether such a termination occurred hinges on the application of *state* law.

A. Congress Enacted the PMPA to Create a National Standard for the Termination and Nonrenewal of Petroleum Franchises.

In enacting the PMPA, Congress established a "single, uniform set of rules" governing the termination and non-renewal of petroleum franchise relationships, which "permeate a nationwide motor fuel distribution and marketing network." S. Rep. No. 731, at 16, 19. To achieve the goal of uniformity, Congress replaced the "uneven patchwork of rules governing franchise relationships which differ from state to state" (*id.* at 19) with a nationwide standard

for termination and non-renewal of franchise relationships. To ensure uniformity, Congress preempted any state laws or regulations governing termination or nonrenewal that are different from the PMPA. 15 U.S.C. § 2806(a)(1).

The uniformity Congress sought serves important goals. Because refiners distribute their fuel nationwide, a uniform regulatory approach permits refiners to operate under a single set of rules, which promotes certainty and efficiency in their franchise relationships. The costs of dealing with unpredictable market conditions are compounded when the legal regime governing the termination and non-renewal of franchise relationships varies from one jurisdiction to another. The higher costs associated with an uncertain and non-uniform legal regime harm both franchisors and franchisees.

B. The Court of Appeals' Decision Precludes Uniformity Because the Viability of a Constructive Termination Claim Depends on State Law.

In this case, the court of appeals held that the dealers had a cause of action under the PMPA for wrongful termination despite the undisputed facts that the dealers continued to operate their franchises without interruption and that Shell neither terminated the dealers' franchises nor notified the dealers of an intent to terminate their franchises. Pet. App. 15a-21a. In particular, the court held that Shell's alleged breach of oral promises to retain a rent subsidy program amounted to a "constructive"

termination of the dealers' franchises because of the "financial hardship" it allegedly caused them. *Id.* at 21a.

Without attempting to ground the concept of constructive termination in the text of the Act, the court held that "the breach of the statutory element of the franchise"—*i.e.*, the contract to use the refiner's trademark, the contract for the supply of motor fuel, or the lease of the premises—"does not have to be a total breach." Pet. App. 18a. Rather, the court held the breach need only constitute "a material change that . . . effectively ended the lease, even though the plaintiffs continued to operate the business." *Id.* The court acknowledged that the doctrine of constructive termination typically requires "an actual severance of the relationship" (*id.*), but reasoned that "requir[ing] an actual abandonment of years of work and investment before we recognize a right of action under the PMPA would be unreasonable." *Id.*

Under the court of appeals' approach, the determination of whether a franchisee was constructively terminated within the meaning of the PMPA turns on the application of *state* law. The basis for the dealers' constructive termination claim is that Shell breached an alleged oral promise to maintain a rent subsidy, notwithstanding a clause in the lease agreement providing that the lease constituted the entire contract and that any amendments to it must be in writing. Applying Massachusetts law, the district court permitted the jury "to consider what the parties said and did concerning the lease" including "actions prior to or contemporaneous with the execution of the written

lease." Pet. App. 14a. Because Massachusetts reserves the determination of integration for the trial court as a question of fact, the court of appeals affirmed the district court's "conclu[sion] that the lease was not an integrated agreement" under Massachusetts law. *Id.* Thus, because Massachusetts law (as applied by the federal courts) permitted consideration of Shell's alleged prior or contemporaneous oral promises in the face of the integration clause, the dealers could establish that Shell committed a material breach of the franchise terms that amounted to a constructive termination under the PMPA. *See* 15 U.S.C. § 2805(c) ("[T]he franchisee shall have the burden of proving the termination of the franchise[.]").

In other states, this question would have been resolved differently. Courts in Ohio and Florida, construing contract language identical to that at issue here, have read the integration clause as foreclosing evidence of alleged oral promises that the rent subsidy would be permanent. *See Casserlie v. Shell Oil Co.*, No. 88361, 2007 WL 1559510, at *7-8 (Ohio Ct. App. May 31, 2007), *aff'd*, 902 N.E.2d 1 (Ohio 2009); *Hazara Enterprises, Inc. v. Motiva Enterprises, LLC*, 126 F. Supp. 2d 1365, 1373-1374 (S.D. Fla. 2000). Other jurisdictions similarly give dispositive effect to a clear integration clause. *See, e.g., Tangren Family Trust v. Tangren*, 182 P.3d 326, 331 (Utah 2008) ("[W]e will not allow extrinsic evidence of a separate agreement to be considered on the question of integration in the face of a clear integration clause."); *Air Safety, Inc. v. Teachers Realty Corp.*, 706 N.E.2d 882, 885 (Ill. 1999) ("[W]here parties formally include an integration

clause in their contract, they are explicitly manifesting their intention to protect themselves against misinterpretations which might arise from extrinsic evidence."). In states applying such a rule, the dealers here could not have succeeded in establishing constructive termination under the PMPA based on Shell's breach of alleged oral promises made before or contemporaneous with the execution of the written lease.

By allowing a cause of action under the PMPA for constructive termination based on a material breach of one of the franchise terms, the court of appeals allowed state law to determine whether the franchisor has effected a termination under the PMPA. Given Congress' goal of replacing the "uneven patchwork of [state] rules" with a "single, uniform set of rules" governing termination of petroleum franchises, S. Rep. No. 731, at 19, that result could not possibly be what Congress intended.

III. An Assignment Does Not Constitute Termination Of A Franchise Under The PMPA Merely Because The Assignee Breaches The Contract Or Because The Assignment Violates State Law.

In recognizing a cause of action under the PMPA for constructive termination, the court of appeals relied on the Fourth Circuit's decision in *Barnes v. Gulf Oil Corp.*, 795 F.2d 358 (4th Cir. 1986). *See* Pet. App. 15a-18a (citing and quoting *Barnes*). *Barnes* set out two theories to justify relief for franchisees claiming, as the dealers did here, that an assignment of their franchises violated their

rights under the PMPA. Neither theory is properly cognizable under the PMPA.

First, *Barnes* held that a "franchisee can obtain relief under the Act if the franchisee [by virtue of an assignment of the franchise] can no longer obtain gasoline at the stipulated franchise price." *Id.* at 362. *Barnes* is incorrect. As explained above, the text, structure, and purpose of the PMPA preclude a cause of action for constructive termination predicated on a breach of contract by the franchisor that does not effect a termination of the franchise. It follows that, contrary to *Barnes* and the court of appeals' decision here, a cause of action does not lie "against the assignor of a franchise when the assignee breaches the franchise." Pet. App. 17a (citing *Barnes*, 795 F.2d at 362). The court of appeals reasoned that permitting a franchisee to pursue a PMPA claim against the assignor when the assignee commits a breach "prevents the assignor/franchisor from shielding itself against liability through the use of another corporation." *Id.* This rationale lacks merit because its premise is flawed: even absent an assignment, the franchisor would not be liable for wrongful termination under the PMPA for a mere breach of contract that did not constitute a termination of the franchise.

Second, *Barnes* held that an assignment that is invalid under state law "is tantamount to a constructive termination of the franchise" in violation of the PMPA. 795 F.2d at 363. The court of appeals embraced that theory in dicta here, stating that "an assignment that is violative of state law, . . . gives rise to a claim under the PMPA against the original franchisor/assignor." Pet. App.

15a-16a. This Court should make clear that the PMPA does not permit a cause of action based on this theory either. Absent such clarification, franchisees may simply recast material-breach claims under the PMPA as termination claims based on assignments in violation of state law. These two assignment-based claims go hand-in-hand because many states, including Massachusetts, *see* Mass. Gen Laws ch. 106, § 2-210 (2009), have incorporated into their statutory schemes language from the Uniform Commercial Code declaring that an assignment that "increase[s] materially the burden or risk" imposed by the contract is invalid. *See* UCC § 2-210 (2004); *see, e.g.*, Tenn. Code Ann. § 47-2-210 (2009); Ohio Rev. Code Ann. § 1302.13(B) (2009); Va. Code Ann. § 8.2-210(2) (2009); Or. Rev. Stat. § 72.2100(2) (2007). Thus, when an assignment results in a change to the gasoline price, or to another statutory element, that is unfavorable to the franchisee, the franchisee will usually proceed under both theories, arguing that a constructive termination has occurred both because the assignment breached a statutory element and because the assignment violated state law.

For example, the plaintiff in *Clark v. BP Oil Co.*, 137 F.3d 386, 390-91 (6th Cir. 1998), argued both that the franchisor constructively terminated his franchise by breaching the supply and lease agreements and that the franchisor assigned the franchise in violation of Tennessee law. Both arguments were based on the same underlying facts: the franchisor's assignment of the franchise to a third party that charged a higher price for gasoline. Similarly, in *Shukla v. BP Exploration & Oil, Inc.*,

115 F.3d 849, 852-53 (11th Cir. 1997), the plaintiff argued that the franchisor constructively terminated his franchise on the theories that "the assignment increased his burdens under the franchise agreement and was therefore invalid under Florida law" and that the assignee's "pricing practices constituted a breach of the supply component of his franchise agreement, resulting in a termination of the franchise." *See also, e.g., Portland 76 Auto/Truck Plaza, Inc. v. Union Oil Co. of Cal.*, 153 F.3d 938, 948 (9th Cir. 1998); *Sawhney v. Mobil Oil Corp.*, 970 F. Supp. 366, 371-72 (D. N.J. 1997), *rev'd*, 173 F.3d 421 (3d Cir. 1998); *Cedar Brook Serv. Station, Inc. v. Chevron U.S.A., Inc.*, 746 F. Supp. 278, 282 (E.D.N.Y. 1990), *aff'd*, 930 F.2d 908 (2d Cir. 1991).

Barnes' conclusion that a franchise assignment in violation of state law terminates the franchise rests on a faulty understanding of the law of assignments. An assignment that violates state law is invalid, but an invalid assignment does not dissolve the original contract between franchisor and franchisee. Rather, the assignment is simply ineffective, and the original contractual obligations between franchisor and franchisee remain. *See, e.g.*, U.C.C. § 2-210 cmt. 3; E. Allen Farnsworth, *Farnsworth on Contracts* § 11.4 (2001); *Restatement (Second) of Contracts* § 317 cmt. a & illus. 2 (1981).[7]

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[7] If the contract prohibits assignments, then the franchisee would have a state-law claim against the franchisor for breach of contract. If the original franchisor no longer exists, then the rules of successor liability would apply.

Because the franchise agreement between the franchisor-assignor and franchisee would remain in force, the *Barnes* court was wrong to conclude that an invalid assignment would terminate the franchise. *Barnes* sought to support its holding by reference to one part of the statutory definition of a franchise. Under that definition, a franchise includes "the unexpired portion of any franchise . . . which is transferred or assigned as authorized . . . by any applicable provision of state law." 795 F.2d at 363 (quoting 15 U.S.C. § 2801(1)(B)(iii)). That definition makes clear that the PMPA governs a franchise that is assigned in accordance with state law, but it does not address franchise assignments that violate state law. Where an assignment is ineffective, the assignor remains bound by the contract, and the agreement between the dealer and the franchisor is thus still a "franchise" within the more general definitions of 15 U.S.C. § 2801(1)(A), (B)(i)-(ii).

The *Barnes* court also relied on Section 2806(b)(1) of the Act, which states:

> Nothing in this subchapter authorizes any transfer or assignment of any franchise or prohibits any transfer or assignment of any franchise as authorized by the provisions of such franchise or by any applicable provision of state law which permits such transfer or assignment without regard to any provision of the franchise.

Barnes, 795 F.2d at 363. The *Barnes* court inferred from this provision that "an assignment that is

unauthorized by state law is prohibited" by the PMPA. *Id.* But Section 2806(b)(1) is an expression of *neutrality* toward state law on assignments. Contrary to *Barnes*, it cannot be read to provide that an assignment prohibited by state law is itself a violation of the PMPA. Nothing in the provision suggests, much less provides, that the PMPA incorporates state law on assignments. If Congress had intended to provide that an assignment in violation of state law constitutes an unlawful termination under the PMPA, it easily could have said so. This Court should thus reject as misguided the *Barnes* court's attempt to infer such intent from various provisions of the PMPA that do not address termination.[8]

IV. The PMPA Does Not Create A Cause Of Action For Constructive Nonrenewal.

For the very reasons that the court of appeals erred in allowing a cause of action for constructive termination, it correctly decided that the PMPA does not provide a cause of action for constructive nonrenewal. Pet. App. 21a-25a (relying on the text and structure of the Act to reject the dealers' constructive nonrenewal claim). Because the PMPA

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[8] Moreover, the *Barnes* court's view that an assignment in violation of state law amounts to a termination under the PMPA is entirely at odds with the PMPA's text and structure, which require actual termination or nonrenewal of the franchise to trigger the protections of the Act. *See* Part I, *supra*. A PMPA cause of action for assignments that violate state law would also undercut the PMPA's goal of national uniformity by expressly resting recovery under the Act on state law. *See* Part II, *supra*.

defines "nonrenewal" as the "failure to reinstate, continue, or extend the franchise relationship," 15 U.S.C. § 2801(14), a franchisee who has signed a renewal agreement cannot claim that a nonrenewal within the meaning of the Act has occurred. Moreover, as it does for franchise termination, the PMPA establishes a detailed set of notice requirements and preliminary relief provisions governing the nonrenewal of petroleum franchises that are nonsensical unless nonrenewal is understood to mean what it says—a severance of the relationship between franchisor and franchisee. *See* 15 U.S.C. §§ 2804 and 2805(b); Pet. App. 22a ("This notice-and-preliminary-relief structure is evidence that Congress intended to limit the reach of the PMPA to cases where either a notice [of nonrenewal] is given or an actual nonrenewal has taken place.") (citing *Abrams Shell v. Shell Oil Co.*, 343 F.3d 482, 489 n.16 (5th Cir. 2003), and *Dersch Energies*, 314 F.3d at 865)). The sections of the Act providing the permissible grounds for nonrenewal likewise presume that an actual nonrenewal will take place. *See* 15 U.S.C. § 2802(b).

The dealers have argued that the court of appeals' rejection of constructive nonrenewal will force franchisees "to choose between accepting an unlawful and coercive contract in order to stay in business and rejecting it and going out of business in order to preserve a cause of action." Petition for a Writ of Certiorari, *Mac's Shell Service, Inc., et al. v. Shell Oil Prods., Inc., et al.*, No. 08-240, 2008 WL 3919440, at *20 (U.S. Aug. 21, 2008). This contention ignores the provisions of the PMPA that protect franchisees from having to make such a

choice. A franchisor that intends not to renew usually must give the franchisee 90 days notice prior to nonrenewal. 15 U.S.C. § 2804(a). Franchisees may then seek a preliminary injunction under the lenient standards set forth in 15 U.S.C. § 2805, which allow them to continue to operate under the preexisting terms while the court decides the merits of their claims. *See* Part I(B), *supra*.

CONCLUSION

The judgment of the court of appeals with respect to the dealers' constructive termination claims should be reversed, and the judgment with respect to the dealers' constructive nonrenewal claims should be affirmed.

Respectfully submitted,

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